FINAL REPORT
OF THE
INTERIM STUDY COMMITTEE ON
SCHOOL FUNDING FORMULA

Indiana Legislative Services Agency
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Interim Study Committee on School Funding Formula

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FINAL REPORT

Interim Study Committee on School Funding Formula

I. STATUTORY DIRECTIVE

The General Assembly enacted P.L.182-2009(ss), SECTION 512, directing the Interim Study Committee on School Funding Formula to study issues related to the school funding formula. The legislation required the Committee to be established by the Legislative Council as a two-year study committee.

II. INTRODUCTION AND REASONS FOR STUDY

Public schools, including charter schools, receive a distribution of money from the state through a tuition support formula enacted by the General Assembly. The money distributed through the tuition formula is not restricted and may be used for any of the purposes of the public schools receiving the distributions. Until 2008, the tuition support formula also regulated the amount of general revenue that could be raised by a school corporation from property taxes. In 2008 (P.L.146-2008), the General Assembly terminated the authority of school corporations to enact a property tax levy for general fund purposes and increased the amount of the state revenue distributed through the tuition support formula to replace the lost property tax revenue. In 2009, additional changes to the tuition support formula were enacted in P.L.182-2009(ss), including changes to reflect the availability of grants authorized in the federal American Recovery and Reinvestment Act (ARRA) of 2009.

III. SUMMARY OF WORK PROGRAM

The Committee heard from 27 witnesses in five meetings. The meetings were held over a two-year period in 2009 and 2010.

2009

The Committee met twice during the 2009 interim between sessions of the General Assembly. The first meeting was held on September 23, and the second meeting was held on October 19.

In the first meeting, the Committee heard testimony from a school superintendent and from various school education associations expressing a need for reform in the school funding formula and various other funding statutes. One person expressed concern that improvements could not be made in the current formula. Several witnesses suggested that the biggest hurdle would be finding additional money to fully fund current programs and to increase the total amount distributed to elementary and high schools.

In the second meeting the Committee heard testimony from: (1) the Center for Evaluation and Education Policy at Indiana University concerning the study the Center was conducting on the issue of school funding adequacy; and (2) from witnesses discussing the law governing the conversion of school corporations from a calendar-year budgeting cycle to a fiscal-year (school-year) budgeting cycle.

2010

The Committee met three times in the 2010 interim. The first meeting was on August 30th. The second meeting was on September 29th. The third meeting was on October 19th.

In the first meeting, the Committee received information summarizing basic school statistics and information, school formulas used by other states, and other potential approaches to state budgeting of tuition support. The Committee took public testimony describing the efficiencies schools made to cope with funding shortages and recommending changes to improve K-12 funding. The Committee heard additional testimony on the subject of converting schools from a calendar-year budget to a fiscal-year budget.

In the second meeting, Superintendent Tony Bennett addressed the Committee concerning school funding. The Committee received additional information about the history of the school funding formula. The testimony covered the complexity index, enrollment changes, the deghoster adjustment, and other formula factors that have led to differences in the amount distributed to public schools per enrolled student. The Committee also received public testimony on various other funding topics.

In the third meeting, the Committee received written information from the Department of Education on the savings and efficiencies undertaken by schools. The Committee also adopted the final report presented by Ed Gohmann, attorney for the committee, by a vote of 11 to 0.

IV. SUMMARY OF TESTIMONY

The Committee heard testimony concerning the following topics.

Indiana's Tuition Support Formula

In the 1970s, the state used an average daily attendance (ADA) count in the school funding formula. In 1975, the state began using a combination of the ADA and the average daily membership (ADM) count. The ADA count was based on the average number of students attending in a 15-day period, and the ADM count is based on the number of students on a fixed day. An enrollment change factor (the "deghoster") was introduced to address the issue of declining attendance. The idea behind the deghoster was to give school corporations with declining enrollment the time to adjust to those enrollment changes.

Various factors that have been used in the school funding formula at various times, including: (1) the training and experience index, (2) flat grants, (3) the minimum guarantee, (4) maximum increase limits, (5) adjustments for enrollment changes, (6) a "bottom-up" adjustment that sets a minimum dollars-per-student funding level, (7) the small-school grant, and (8) the complexity index. The various factors were added to address different policy goals.

These factors, over time, have had the result of producing differences among school corporations in the amount of money received per student. School corporations with similar demographics do not all receive the same amount of funding per student.

In 2008, the General Assembly enacted legislation terminating the authority of a school corporation to impose a general property tax levy for the school general fund. However, since 1973 there has been authority for a school corporation to seek a referendum to impose an additional property tax levy for the operation of schools. The referendum authority was not repealed. Some witnesses expressed concern that the referendum provisions will increase inequities in per-pupil funding if the voters in only some school corporations approve referendum levies.

Student-Based Adjustments

The Indiana school tuition support formula has a number of student-based adjustments that increase the amount of money that a school corporation receives above the foundation amount provided for all students. The tuition support formula provides an additional grant to school corporations with students that have a disability status or are enrolled in a career or technical education program. An adjustment to the basic foundation amount received for all enrolled students, known as the complexity index adjustment, increases funding for school corporations with higher numbers of students with low income.

The complexity index is calculated using the number of students in a school corporation who qualify for the free or reduced lunch program. Other factors have been included in the index in past years. However, eligibility for the free and reduced lunch program has been statistically determined to be a good indicator of the need for school corporations to spend additional funds to meet the needs of students who have difficulty learning.

Alternative Tuition Support Approaches

The Committee received a broad range of suggestions for changes in the tuition support formula. The suggestions included specific proposals, such as increasing the foundation amount, modifying the complexity index, and adding a performance improvement index. The suggestions also included requests that the tuition support formula be adjusted to: (1) be more transparent and understandable; (2) be more equitable; and (3) result in school districts with similar demographics receiving similar funding. There were requests for full funding of full-day kindergarten, summer school, and 12-month schools.

A review of the practices in other states prepared by the EPE Research Center (with the District of Columbia being treated as a state for the purposes of the study) indicates that 38 of 51, or 76.0%, of states use a foundation funding formula to determine funding for school districts. All states that use a foundation funding formula have a specific allotted per-pupil expenditure. Sixteen of 38, or 42.0%, of states and territories that use a foundation formula also use an equalizing formula. Eight of the 38 states that use a foundation-type funding formula, or 21.0%, only use a funding formula to allocate school funds. Forty-seven of 51, or 94.0%, of states use more than one formula to allocate school funds.

State practices differ with respect to the types of student-based adjustments that are used to increase the amount of money received by particular school districts. Although none of the states use all of the possible adjustment facts, the student-based factors used in the various states to adjust the amount distributed to a particular school include disability status, English language learner status, low income, grade level, career and technical Education, academically at-risk status, as well as other factors. Twenty-two of 51, or 43.1%, of states provide extra funding for other purposes. Four of 51, or 7.8%, of states provide funding for six of the seven categories.

Funding Levels

Four different approaches are generally used to estimate the level of expenditures needed to meet educational goals. They include: (1) the professional judgment model, (2) the evidence-based model, (3) the cost-function model, and (4) the successful schools model.

There have been 162 lawsuits nationwide concerning school funding (110 related to adequacy and 52 related to equity). There have been three school funding lawsuits filed in Indiana. One is pending at the trial court level. The last case heard by the Indiana Supreme Court was Bonner ex rel. Bonner v. Daniels, 907 N.E.2d 516 (Ind.,2009). The Court determined in Bonner that the Education Clause of the Indiana Constitution did not impose an affirmative duty on the General Assembly to establish a particular standard of quality and the state's public education finance scheme did not violate the Equal Privileges or Due Course of Law Clauses of the Indiana Constitution.

Many Indiana public schools are finding steps need to be taken to produce balanced budgets. Some witnesses recommended that the total amount of money distributed to public schools be increased to maintain schools and improve student performance. The witnesses suggested that the amount distributed to a public school be based on the actual costs incurred by the public school to meet the educational needs of the children enrolled in the public school. Other witnesses discussed the steps that are being taken to control costs.

Control of Health Care Costs

The Department of Education prepared and distributed to school corporations a "Citizen's Checklist" of ideas for cost reductions. One of the suggestions is for the governing body of a school corporation to "review and compare their health plan to the state plan for cost effectiveness, level of coverage, appropriate deductibles or adjusting benefits to their current plan."

A Department of Education survey reveals that 90% of school corporations have recently conducted a review of the health care plans offered to employees. Some school corporations will receive significant savings from joining the state health car plan. Five school corporations have switched to the state plan with an expected savings of $3.5 million. Other school corporations incur lower costs under their current health care plans than would be incurred if they converted to the state plan. One estimate indicated that the 13 members of a health care consortium would incur an additional $4.38 million in expenditures if they were to convert to the state plan. In some cases, heath care benefit costs may be higher as a result of negotiated agreements with employees who agreed to accept a lower salary in order to fund better health care benefits.

Other Cost-Control Measures

School business officers have had an ongoing discussion for a number years about potential cost-saving and cutting strategies. A survey of school management practices and testimony indicate that school corporations are implementing a broad range of cost-cutting measures, including closing school buildings, freezing salaries, reducing employer fringe benefit contributions, reducing personnel positions by such initiatives as changing school schedules, outsourcing custodial work, and accepting hospital assistance in finding volunteer nurses, lengthening computer and equipment replacement cycles, and reducing insurance and utility costs. A number of these initiatives were implemented with the cooperation of employees who agreed to renegotiate employment contracts.

The Committee received testimony that Oklahoma, Texas, and Virginia schools have undertaken school efficiency studies. In Virginia, for example, local school districts pay 25% of the cost of the review and the state pays the remaining 75% (although if the local district does not implement a certain amount of the efficiency recommendations made during the review, the local district must pay more).

Fiscal-Year Budget

In 1996, the General Assembly authorized the Department of Education to select up to 10 school corporations to participate in a pilot program to budget school expenditures on a fiscal-year basis rather than a calendar-year basis (P.L.50-1996, SECTION 18). The initial legislation provided for all school corporations to convert to a fiscal-year budget in 1999 and for the pilot program to terminate on July 1, 1999. The General Assembly subsequently enacted legislation to delay the conversion of all schools to a fiscal-year budgeting cycle. The pilot program was extended for an indefinite period (P.L.96-2000, SECTION 9). In 2001, the General Assembly gave authority to the governing body of the South Bend Community School Corporation to elect to convert to a fiscal-year budget cycle (P.L.178-2001, SECTION 2). In 2010, the General Assembly eliminated the mandate that all schools convert to a fiscal-year budget cycle and authorized each school corporation to make its own determination as to whether the school corporation would use a fiscal-year budget cycle or calendar-year budget cycle (P.L.111-2010). Two schools are using a fiscal-year budget cycle: Metropolitan School District of Warren Township and Eastern Pulaski Community School Corporation.

Several school business managers suggested that requiring schools to convert to a fiscal-year budget cycle would cause a financial hardship on schools with rising student counts unless the General Assembly altered the tuition support formula and distribution cycle to distribute money for the additional students at the beginning of the fiscal year. Testimony was received suggesting that the idea had been thoroughly discussed and that it is time to move on without any change in current law.

V. COMMITTEE FINDINGS AND RECOMMENDATIONS

The Committee made the following findings of fact.

<u>School Funding Formula</u>

The committee studied different methods of funding schools used in other states but did not find any that appeared to be clearly superior to the approach that has been used in Indiana. Given the state budget crisis and the impact of multiple federal grants on school funding, this does not appear to be a good time to adopt a fundamentally different approach to the school formula.

Over the past 10 years, Indiana's school funding formulas have broken any ties that may have existed between the property wealth in a school district and per-pupil funding. This is an important achievement that has helped Indiana ward off costly lawsuits based on equity that have plagued several other states. In that regard at least, the approach Indiana has taken on school funding has served the state well.

Thirty-eight states, including Indiana, have a foundation component as part of their school formula.

Referendums for school general fund spending and interfund transfers to date do not appear to have led to any significant funding inequities among school corporations. The General Assembly needs to monitor referendums and interfund transfers to ensure that over time they do not create funding inequities and undo the equalization progress of the state over the last 20 years.

The Committee did not determine how much additional per-pupil funding (beyond the foundation amount) is needed to compensate for the increased cost of educating at-risk children.

Indiana's school funding formulas have recognized that it takes additional funds to educate at-risk children and have dedicated significant additional dollars to schools with high numbers of at-risk students. The complexity index in the school formula increased regular tuition support foundation funding by $1 billion for CY 2010 to reflect the additional costs associated with at-risk students.

About 41% of students enrolled in school corporations in Indiana were eligible for free or reduced lunches in 2010.

Since 1999 Indiana's school formulas have included "reghosters" (funds distributed to a school for students no longer enrolled in that school) in order to help the school transition to declining enrollments. Indiana's 2009 school funding formula included $93 million for a five-year reghoster, while the 2010 school funding formula included $65 million for a three-year reghoster. Reghosters can be modified by other formula factors to reduce the net impact that the reghosters would otherwise have.

Revenue per ADM (average daily membership) varies widely among school districts and charter schools, but these differences are not always accounted for by differences in schools' complexity indices. Only about 40% of the variation is explained by the complexity index.

In 2009 the median school general fund and Federal Stabilization Fund revenues per ADM was $7,107 per ADM. These figures ranged from a low of $5,762 per ADM to a high of $16,416 per ADM. If the top and bottom 5% of schools are removed from the distribution to remove the extremes, then the range becomes a low of $6,037 per ADM and a high of $9,990 per ADM.

In 2009 the median dollars per ADM for total funding (including school general fund, Federal Stabilization Fund, federal Title Funds, and property taxes) was $11,161 per ADM. These figures ranged from a low of $6,157 per ADM to a high of $25,586 per ADM. If the top and bottom 5% of schools are removed from the distribution to remove the extremes, then the range becomes a low of $9,045 per ADM and a high of $14,988 per ADM.

For 2010 the gross revenue reduction to schools due to circuit breaker credits will be $148.5 million. However, the amount of this loss is reduced by state grants of $50 million. Therefore, the net cost to schools from circuit-breaker credits is expected to be $98.5 million (or approximately 3.7% of total school levies or 9.5% of nondebt school levies). Circuit-breaker credits do not directly impact school general funds.

Many of the schools with the largest circuit breaker losses are urban schools that have declining enrollments and are closing facilities.

Some schools have done a credible job cutting administrative costs to help save teachers' jobs. The Department of Education has provided a checklist of potential reductions, and schools have implemented their own plans. Actions taken include cutting staff, reducing professional development expenditures, reducing nonrevenue-generating extra curricular programs, outsourcing custodial services, reducing travel, selling unneeded buildings, more collaborative procurement, and reviewing health care plans. The average cut is about $1.5 million.

Employee Health Insurance

Several school corporations have experienced significant savings by electing to join the state's health insurance program.

The cost for existing health insurance programs for some school corporations and consortia appears to be lower than the cost of the state's health insurance program.

Miscellaneous

Enrollment in Indiana schools grew from 980,900 to 998,042 from 2005 to 2010 - an increase of 17,142 students, or about 1.78%.

The number of teacher full-time equivalents increased from 59,290 to 60,168 from 2005 to 2010 - an increase of about 1.5%.

Average ADM per teacher fell from about 16.5 students per teacher in 2005 to 16.3 students per teacher in 2010 - a decrease of about 1.1%.

The statewide Student Instructional Expenditures ratio (Dollars to the Classroom) for Indiana schools in 2008-09 was 57.8%. This figure trailed the United States average by about five percentage points. Every percentage point improvement in this figure equates to about $110 million of additional dollars to Indiana classrooms.

The average salary of a teacher in an Indiana public school increased from $46,611 to $50,270 from 2005 to 2010 - an increase of about $3,659, or 7.9%.

Total property tax levies for Indiana schools has decreased from $4.0 billion in 2005 to $2.7 billion in 2010 - a decrease of about $1.3 billion, or 32% (largely due to the state's assumption of the remaining school general fund costs).

The Committee made the following recommendations:

The General Assembly should monitor school general fund referendum results and interfund transfers to ensure they do not lead to per-pupil funding inequities.

The General Assembly should monitor the impact on school corporations of special U.S. Department of Education grants, such as the stimulus funds and Education Jobs Fund dollars.

The cost of the state's health insurance programs and employer/employee cost-sharing should serve as a general guide for schools in determining the appropriate costs of health care. When addressing questions about health insurance costs for schools and the state, analysis should be done to make sure there is also a fair comparison of coverages and benefits.

The school formula should include factors to address the costs of programs for students with special needs.

During committee deliberations additional questions arose concerning the foundational structure of education in Indiana, excluding funding but including topics such as the structure and relationship of preschool to primary education to higher education, how schools are organized, and the school calendar. While these questions are outside the scope of the study committee, they are worthy of consideration and might be topics for consideration for the Education Roundtable or some other committee.

W I T N E S S   L I S T

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